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signed 7-23-01

**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF KANSAS**

**In re:**

**THOMAS ALAN VONTHAER,**

**DEBTOR.**

**CASE NO. 99-42819-13  
CHAPTER 13**

**ORDER SUSTAINING TRUSTEE'S OBJECTION**

**TO CREDITOR'S CLAIM FOR ATTORNEY FEES**

This matter is before the Court on the Chapter 13 Trustee's objection to a portion of the claim filed by PNC Mortgage Corporation of America ("PNC"). Trustee Jan Hamilton appears *pro se*. PNC appears by counsel Steven L. Crouch. The Court has reviewed the relevant materials and is now ready to rule.

**FACTS**

The following facts are not controverted. In March 1992, debtor Thomas Alan VonThaer borrowed money from Kansas Home Mortgage, Inc., secured by a mortgage on his home. That company apparently assigned the note and mortgage, without recourse, to Sears Mortgage Corporation, which is now known as PNC. PNC now identifies itself as the loan servicing agent for the owner and holder of the note and mortgage; the owner and holder does not appear to be identified in any of the pleadings. The mortgage appears to have been insured by the United States Department of Housing and Urban Development ("HUD") under the National Housing Act.

The debtor filed a chapter 13 bankruptcy petition on December 13, 1999, and his plan was confirmed the following September. In his schedules, the debtor valued his house at \$48,000, and indicated that PNC had filed a foreclosure action against him. PNC filed a proof of secured claim for almost \$46,000, including \$1,131.38 in prepetition legal fees and costs as part of an arrearage it asserts the debtor owes. PNC has not indicated whether these fees and costs were incurred in the foreclosure action. Apparently, PNC's claim is oversecured. The trustee objected to the prepetition legal fees and costs that PNC included in its claim.

PNC's defense of its claim for these fees and costs has been something of a moving target. In its initial response to the trustee's objection, PNC pointed to paragraph 10 of the mortgage, which provides in pertinent part:

**Reinstatement.** Borrower has a right to be reinstated if Lender has required immediate payment in full because of Borrower's failure to pay an amount due under the Note or this Security Instrument. This right applies even after foreclosure proceedings are instituted. To reinstate the Security Instrument, Borrower shall tender in a lump sum all amounts required to bring Borrower's account current including, to the extent they are obligations of the Borrower under this Security Instrument, foreclosure costs and reasonable and customary attorneys' fees and expenses properly associated with the foreclosure proceeding. . . .

Then, PNC filed a brief in support of its response, and this time relied on paragraph 6 of the mortgage, which provides in pertinent part:

**Charges to Borrower and Protection of Lender's Rights in the Property.** Borrower shall pay all governmental or municipal charges, fines and impositions that are not included in paragraph 2. Borrower shall pay these obligations on time directly to the entity which is owed the payments. If failure to pay would adversely affect Lender's interest in the Property, upon Lender's request Borrower shall promptly furnish to Lender receipts evidencing these payments.

If Borrower fails to make these payments or the payments required by paragraph 2, or fails to perform any other covenants and agreements contained in this Security Instrument, or

there is a legal proceeding that may significantly affect Lender's rights in the Property (such as a proceeding in bankruptcy, for condemnation or to enforce laws or regulations), then Lender may do and pay whatever is necessary to protect the value of the Property and Lender's rights in the Property, including payment of taxes, hazard insurance and other items mentioned in paragraph 2.

Any amounts disbursed by Lender under this paragraph shall become an additional debt of Borrower and be secured by this Security Instrument. These amounts shall bear interest from the date of disbursement, at the Note rate, and at the option of the Lender, shall be immediately due and payable.

The payments required under paragraph 2 of the mortgage are for property taxes and special assessments, leasehold payments or ground rents, hazard insurance, and HUD mortgage insurance.

After the trustee responded to PNC's supporting brief, PNC filed a reply in which it relied on still another paragraph of the mortgage, paragraph 8, which reads:

**Fees.** Lender may collect fees and charges authorized by the Secretary.

The "Secretary" referred to is the Secretary of HUD. PNC asserts that HUD issued a letter in 1998 that allows a mortgagee to charge fees and costs for a foreclosure action, and fees and costs "to remove file from bankruptcy."

## DISCUSSION AND CONCLUSIONS

PNC concedes that before 1994, Kansas law prohibited provisions in mortgages (and many other types of contracts) that would require borrowers to pay their lender's attorney fees, declaring such provisions to be "null and void." K.S.A. 58-2312 (1983 Ensley). Although the statute was amended effective July 1, 1994, to permit such provisions, 1994 Kan. Sess. L. ch. 276, §3 (codified at K.S.A. 58-2312), PNC also concedes that the Kansas Court of Appeals has ruled that this amendment applies only prospectively, to contracts made after July 1, 1994. *See Ryco Packaging*

*Corp. v. Chapelle Int'l*, 23 Kan. App. 2d 30, 42-46 (1996), *rev. denied* 261 Kan. 1086 (1997). As PNC notes, at least one federal district court judge has followed *Ryco* on this point. *Baxter State Bank v. Bernhardt*, 985 F.Supp. 1259, 1270-71 (1997). This Court agrees that the amendment to 58-2312 applies only prospectively and therefore, Kansas law voided any provision in PNC's mortgage that tried to require the debtor to pay PNC's attorney fees.

Nevertheless, although the Bankruptcy Code did not apply to PNC's relationship to the debtor until the debtor filed for bankruptcy, PNC contends §506(b) of the Code allows it to recover from the debtor attorney fees and expenses it incurred before the debtor filed for bankruptcy. To support this argument, PNC relies on *In re American Metals Corp.*, 31 B.R. 229 (Bankr. D. Kan. 1983), and *In re Hyer*, 171 B.R. 67 (Bankr. W.D. Mo. 1994) (Missouri judge applying Kansas law to Kansas mortgage). In each of these cases, the court ruled that §506(b) authorized an oversecured creditor to recover attorney fees as allowed under its contract even if applicable state law prohibited such a recovery. 31 B.R. at 233-35; 171 B.R. at 70-71. In addition, each court appears to have allowed the creditor to recover some prepetition attorney fees. *See* 31 B.R. at 235-36; 171 B.R. at 69, 71. However, neither court actually said anything about the propriety of allowing prepetition fees under §506(b), or indicated that any party had argued that prepetition fees presented a different question than postpetition ones. To the extent the decisions can be construed to have held that prepetition fees are recoverable under §506(b) despite contrary law that applied before the debtor filed for bankruptcy, this Court must disagree with them.

Section 502(b) of the Bankruptcy Code provides that, when an objection to a filed proof of claim is made, the court is to determine the amount of the claim as of the date of the filing of the petition

and allow it in that amount “except to the extent that—(1) such claim is unenforceable against the debtor and property of the debtor, under any agreement or applicable law for a reason other than because such claim is contingent or unmatured.” The pre-1994 version of K.S.A. 58-2312 made any contractual provision for attorney fees void and unenforceable, so, as directed by §502(b)(1), the portion of PNC’s claim that is for prepetition legal fees and expenses must be disallowed. As the Tenth Circuit explained in *Rushton v. State Bank (In re Gledhill)*, 164 F.3d 1338, 1340 (10th Cir. 1999), §506(b) controls a creditor’s right to recover interest, fees, costs, and charges that accrue *after* a bankruptcy petition is filed. *See also 4 Collier on Bankruptcy, 15th Edition revised*, ¶506.04 (Lawrence P. King, ed., 2001) (“Section 506(b) governs the allowance of *postpetition* interest, fees, costs and charges as part of a secured claim.” (Emphasis added)). As indicated by §502(b)(1), on the other hand, the creditor’s right to recover such items that accrued *before* bankruptcy is controlled by the non-bankruptcy law that applied before the debtor filed for bankruptcy.

Even if §506(b) could be applied to allow prepetition legal fees, the Court would not allow them to PNC here. Section 506(b) provides:

To the extent that an allowed secured claim is secured by property the value of which . . . is greater than the amount of such claim, there shall be allowed to the holder of such claim, interest on such claim, and any reasonable fees, costs, or charges provided for under the agreement under which such claim arose.

Attorney fees are allowable under this provision only if the parties’ contract permits the secured creditor to recover them from the debtor. *See United States v. Ron Pair Enterprises, Inc.*, 489 U.S. 235, 241-42 (1989). As indicated above, in different pleadings, PNC relied on three different

paragraphs in the mortgage as requiring the debtor to pay its attorney fees. A careful review of those paragraphs reveals that none of them in fact do so.

The first paragraph PNC relied on, paragraph 10, is the only one of the three that actually mentions attorney fees. However, the provision would require the debtor to pay PNC's attorney fees only if he were reinstating the note and mortgage pursuant to paragraph 10 after PNC had required immediate payment in full because the debtor had defaulted on his payment obligations. PNC has not supplied anything to show it has required immediate payment, nor has it suggested that the debtor is trying to reinstate the mortgage as permitted under paragraph 10. Even more significantly, the paragraph states such fees would have to be paid only "to the extent they are obligations of the Borrower under this Security Instrument," indicating that the fees would be required under this provision only if some other provision in the mortgage made them an obligation of the debtor. So by itself, this paragraph does not impose an obligation on the debtor to pay PNC's attorney fees.

The second paragraph PNC relied on, paragraph 6, mentions bankruptcy, and PNC apparently referred to it for this reason. However, the payment obligations the paragraph imposes on the debtor clearly concern items such as taxes and insurance, not attorney fees PNC might incur in the course of enforcing or collecting on the mortgage. While legal proceedings such as bankruptcy are mentioned, the paragraph merely authorizes PNC to pay tax, insurance, and other similar obligations when necessary because of a legal proceeding to protect its rights in the mortgaged property. If PNC pays under this paragraph, the debtor is obliged to reimburse whatever PNC paid, but the description of the items covered is simply not broad enough to include PNC's attorney fees.

The last paragraph PNC relied on, paragraph 8, permits PNC to collect fees and charges authorized by the Secretary of HUD. PNC then cites a "Mortgagee Letter" issued by HUD on

September 22, 1998, that concerns the amount of attorney fees that HUD will allow mortgagees to include in “Single Family Mortgage Insurance Claims.” (Although PNC did not supply a copy of HUD’s letter, the Court was able to obtain a copy from HUD’s Internet Web site at: “www.hudclips.org”.) The letter contains no indication that it concerns fees and charges that a mortgagee may collect from its debtor. Instead, the letter indicates that it concerns attorney fees that HUD will pay to mortgagees filing Single Family Mortgage Insurance Claims. For example, the letter states: “Historically, the Department has not published a reimbursement schedule for attorney fees. . . . However, HUD has always reserved the right to reimburse only those costs which it considers to be reasonable and customary.” This indicates the letter is talking about attorney fees HUD will pay to the mortgagee, not fees the debtor must pay to the mortgagee. The letter also refers to HUD Handbook 4330.4 (“Handbook”), issued in September 1994 (also available at [www.hudclips.org](http://www.hudclips.org)). The Handbook contains a foreword that reads in pertinent part:

The Department of Housing and Urban Development (HUD) is authorized by the National Housing Act to insure approved single family housing mortgages made by HUD-approved lending institutions (mortgagees). . . .

When it becomes necessary for mortgagees to apply for benefits under this insurance program, HUD attempts to pay all properly filed claims quickly, fairly and accurately. . . .

Mortgagees do not furnish receipts for expenses with their initial application for benefits, but are required to maintain a complete claim file that fully supports their claim. The claim file must contain all receipts, records, accounts and any other documentation necessary to verify the accuracy of the claim and is subject to audit by the Department. HUD has developed quality assurance requirements for mortgagees to follow in the claim preparation and submission process. Mortgagees are expected to comply with these requirements and use care in preparing their claims for insurance benefits. . . .

This Handbook 4330.4 REV-1, FHA Single Family Insurance Claims, incorporates all outstanding single family claim policy listed on pages I through IV and is designed to provide easy-to-use instructions for the submission of FHA single family insurance claims (except for Home Equity Conversion Mortgages). The handbook provides instructions for the preparation

and submission of Form HUD-27011, Single Family Application for Insurance Benefits, and the actions to be taken (e.g., conveying property or assigning the mortgage to HUD) in order to obtain insurance benefits. . . .

The mortgagee letter indicates the attorney fees it applies to are to be claimed on Form HUD-27011, the one mentioned in the Handbook. The National Housing Act (“NHA”) referred to in the Handbook’s foreword appears at 12 U.S.C.A. §1701, *et seq.* Section 1703(a) of the NHA explains that, “The Secretary [of HUD] is authorized and empowered upon such terms and conditions as he may prescribe, to insure banks, building and loan associations, installment lending companies, and other such financial institutions . . . against losses which they may sustain as a result of loans and advances of credit, and purchases of obligations representing loans and advances of credit.” Section 1709 of the NHA authorizes HUD to insure eligible mortgages, and HUD’s single family mortgage insurance is provided to mortgagees like PNC under this power. Thus, the letter to mortgagees that PNC relies on concerns attorney fees that HUD may pay to a mortgagee like PNC under its mortgage insurance coverage, not fees that PNC may recover from the debtor under the mortgage. The Court is convinced that the mortgagee letter cannot be construed to authorize PNC to recover attorney fees from the debtor.

The Court concludes that PNC may not recover its prepetition attorney fees from the debtor because: (1) §506(b) does not authorize an oversecured creditor to recover prepetition fees; and (2) PNC’s mortgage does not obligate the debtor to pay PNC’s attorney fees. Consequently, the trustee’s objection to PNC’s claim is hereby sustained.

IT IS SO ORDERED.

Dated at Topeka, Kansas, this \_\_\_\_\_ day of July, 2001.



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JAMES A. PUSATERI  
CHIEF BANKRUPTCY JUDGE